U.S. Department of Agriculture
Office of the Hearing Clerk
Room 1081
14th & Independence Ave., SW
Washington, D.C. 20250

Re: Filing of Brief for June 26-27, 2001 USDA Hearing in Bloomington, MN

USDA/Agricultural Marketing Service/Dairy Programs:

Please consider this a brief filed in regard to the June 26-27, 2001 federal hearing held in Bloomington, Minnesota regarding pooling issues for the Upper Midwest Marketing Area.

This brief concerns the decision by the Administrative Law Judge not to include Exhibit #34, entered during my testimony at the hearing, as evidence that USDA must consider in its review. Exhibit #34 is a 1977 Consent Decree between the United States Department of Justice and Mid-America Dairymen, Inc. Over objections from the attorney for Dairy Farmers of America (successor cooperative to Mid-Am), the Administrative Law Judge declined to receive it into evidence. (Page 301, lines 20-25 of the transcript.) However, Exhibit #34 was included in the hearing record.

Mr. Beshore, DFA’s attorney, objected to Exhibit #34 as having “no pertinence to this proceeding.” (Page 298, lines 15-16 of the hearing transcript.)

I contend that in fact, the 1977 Consent Decree is relevant evidence because:

608 (7) (A):
   The general precept found under “Terms Common to All Orders”—608 (7) (A) directs the USDA Secretary in the following manner:

   “(7) In the case of the agricultural commodities and the products thereof specified in subsection (2) orders shall contain one or more of the following terms and conditions:
      “(A) Prohibiting unfair methods of competition and unfair trade practices in the handling thereof.”


ADDITIONAL REVENUES GAINED BY DFA’S PRACTICE OF POOLING CALIFORNIA MILK ON ORDER 33 CONSTITUTE AN “UNFAIR METHOD OF COMPETITION” AND AN “UNFAIR TRADE PRACTICE,” AS DEFINED BY 608 (7) (A).

1977 Consent Decree:

The 1977 Consent Decree (Civil Action No 73 CV 661-W-1) is current legal document, administered by the United States District Court for the Western District of Missouri. Portions of the Consent Decree remain in force. In the hearing record, the Consent Decree is Exhibit #34. DFA is bound by the current provisions of the 1977 Consent Decree.

Failure to follow the binding portions of the 1977 Consent Decree by DFA is a violation of federal law.

Part IV, Section (C) of the 1977 Consent Decree is the relevant portion for this discussion, which reads:

“Defendant is hereby enjoined and restrained from:

“(C) qualifying milk for participation in federal milk marketing order pools with a purpose of suppressing the uniform price paid to producers participating in a federal milk marketing pool in order to force, coerce or induce such producers who are not members of defendant or join defendant or to cease selling milk in competition with defendant:”

On the proposal to prohibit pooling of milk on the Upper Midwest Order that is already being pooled on a State milk marketing order, it is commonly acknowledged that DFA is one of the major parties involved in pooling California milk on Order 30.

Evidence presented in the June 26-27 hearing established that from October 2000 through May 2001, dairy farmers pooled on the Upper Midwest milk marketing order lost between $11 and $12 million in milk income, due to the “drain” upon the Producer Price Differential by California milk pooled on the order (caused in part by DFA’s actions).

In my opinion, DFA’s pooling California milk supplies on Order 30 is a clear violation of Part IV, Section (C) of the 1977 Consent Decree, by reducing the prices received by producers whose milk is pooled on the Upper Midwest order. Thus, as an apparent Consent Decree violation, DFA’s actions constitute “unfair methods of competition and unfair trade practices” defined by 608 (7) (A).

Further, Part III of the 1977 Consent Decree notes that:

“The provisions of this Final Judgment shall apply to defendant and each of its directors, officers, agents, employees, subsidiaries, successors, assigns, and their subsidiaries, and too all persons in active concert or participation with any of them who receive actual notice of this Final Judgment by personal service or otherwise.”
Since Land O'Lakes, which owns the former Kraft cheese plant at Melrose, Minnesota jointly with DFA, would be considered "in active concert" with DFA, the precepts of exclusionary behavior defined by the 1977 Consent Decree extend to Land O'Lakes personnel, in my opinion. LOL also pools large volumes of California milk on the Upper Midwest milk order, depressing prices received by all farmers.

As supplementary proof, I am including an eight-page, undated document from DFA's pre-merger period (fall 1997) titled, "Dairy Farmers of America, Inc. Statement of Terms for the Merger." On page 4 of that document is found a heading titled, "Potential Disadvantages of the Merger." The second-listed "Potential Disadvantage" reads:

"DFA will be subject to the restrictions of the antitrust consent orders currently applicable to AMPI, Mid-Am, and WDCI."

CONCLUSIONS:

- Under the "Terms Common to All Orders," the USDA Secretary is obliged by 608 (7) (A) to prohibit unfair methods of competition and unfair trade practices.
- Parts III and IV of the 1977 Consent Decree are currently binding upon Dairy Farmers of America, which inherited the obligation from its successor cooperative, Mid-America Dairymen, Inc.
- DFA is actively pooling large quantities of California milk on the Upper Midwest federal milk order.
- Large quantities of California milk pooled each month on Order 30 are depressing prices received by dairy farmers whose milk is priced by Order 30.
- Violation of the 1977 Consent Decree by DFA (and others) constitutes an "unfair trade practice" listed under 608 (7) (A).
- USDA should consider Exhibit #34 in the evidence while the Secretary renders the decision on the June 26-27 milk order hearing. The 1977 Consent Decree is a relevant document for these deliberations.

Sincerely,

Peter L. Hardin
608/455-2400

Enclosure: 8-page document: "Dairy Farmers of America, Inc." "Statement of Terms of Merger"
Dairy Farmers of America, Inc.

Statement of Terms for the Merger

of

Associated Milk Producers, Inc.
Mid-America Dairymen, Inc.
Milk Marketing Inc.

&

Western Dairymen Cooperative, Inc.
member numbers (% of total): 22,000
member milk (% of total): 32.5 billion
corporate board members: 36
This Joint Statement of Terms is dated September 26, 1997.

Summary

This Statement of Terms is provided by the Consolidation Steering Committee in connection with the proposed combination of the Southern Region of Associated Milk Producers, Inc., a Kansas cooperative marketing association ("AMPI"), Mid-America Dairymen, Inc., a Kansas cooperative marketing association ("Mid-Am"), Milk Marketing Inc., an Ohio cooperative association ("MMI"), and Western Dairymen Cooperative, Inc., a Colorado cooperative marketing association ("WDCI"), into a single Kansas cooperative marketing association to be known as Dairy Farmers of America, Inc. ("DFA"). Each cooperative association may be referred to individually as a "Cooperative" and collectively as the "Cooperatives". The "Consolidation Steering Committee" is composed of the President or Chairman and one or more directors from each of the participating Cooperatives.

The Boards of Directors of the Cooperatives have reviewed the terms of the merger and have voted in favor of combining their respective operations to increase efficiency, enhance profitability and expand markets for member milk. The Board of Directors of each of the Cooperatives recommends that its members/delegates vote in favor of the proposed merger.

DFA will be incorporated in Kansas and operated as a cooperative marketing association. Copies of DFA's proposed Articles of Incorporation and Bylaws are available from your Cooperative as listed on the last page. The permanent Board of Directors of DFA will consist of 36 members drawn from six geographic Areas shown on the Map. The equity accounts of each member of a participating Cooperative will become a capital account of DFA on a dollar-for-dollar basis. No member will have personal liability for the debts of DFA.

Milk volume and the number of members in an Area will be given equal weight in the allocation of board seats among Areas. Each of the six Areas will have an Area Council to monitor business in the Area. Areas will be subdivided into smaller geographic units to enhance local input. Each Area will be responsible for all costs relating to the governance structure in that Area. An elected delegate body will represent the members with one delegate for each 50 farm units.

DFA will operate under a base capital plan (see page 10 for the details). DFA will have two national value-added divisions (manufacturing and bottling), the profits of which will be allocated among the six Areas. Corporate expenses will be allocated to the divisions and areas based upon usage of corporate services.

Further information and copies of any of the documents referenced in this Statement of Terms may be obtained from your Cooperative. This Statement of Terms is qualified in its entirety by the more detailed information contained in the documents referenced to herein.

The Cooperatives

Associated Milk Producers, Inc. ("AMPI")

Information concerning the business and operations of AMPI can be found in its Annual Report for the year ended December 31, 1996 and supplemental financial statements for the six months ended June 30, 1997, copies of which may be obtained from your Cooperative.

Only the Southern Region of AMPI will participate in the combination transaction. Prior to the merger, AMPI will distribute the assets, liabilities, business and operations of its Southern Region as currently conducted (the "Southern Region") to a newly formed Kansas cooperative marketing association to be known as Southern AMPI, Inc. ("Southern AMPI"), which will be owned and controlled by the members of the Southern Region. Southern AMPI will merge into DFA.

Mid-America Dairymen, Inc. ("Mid-Am")

Information concerning the business and operations of Mid-Am can be found in its Annual Report for the year ended December 31, 1996 and supplemental financial statements for the six months ended June 30, 1997, copies of which may be obtained from your Cooperative.

Prior to the merger described below, Mid-Am will adopt the DFA Articles of Incorporation. As a result, Mid-Am will change its name to Dairy Farmers of America, Inc. and Mid-Am will become DFA.

Milk Marketing Inc. ("MMI")

Information concerning the business and operations of MMI can be found in the Annual Report for the year ended June 30, 1997, copies of which may be obtained from your Cooperative. MMI will merge into DFA.

Western Dairymen Cooperative, Inc. ("WDCI")

Information concerning the business and operations of WDCI can be found in its Annual Report for the year ended June 30, 1997, copies of which may be obtained from your Cooperative. WDCI will merge into DFA.

Dairy Farmers of America, Inc. ("DFA")

The combination of Southern AMPI, MMI, WDCI, and Mid-Am will be effected by the merger of Southern AMPI, MMI, and WDCI into DFA, following a vote by Mid-Am to change its Articles of Incorporation. DFA will be the...
surviving corporation in the merger. As a result of the merger, DFA will establish new bylaws. A copy of the Bylaws is available from your Cooperative. Following the merger, each member of Southern AMPI, Mid-Am, MMI, and WDCI will be a member of DFA. Each member’s equity account with their current Cooperative will be transferred to a capital account of the same dollar value with DFA. DFA’s Capital Plan is described beginning on page 10.

The Merger

On September 9, 1997, AMPI, Mid-Am, MMI, and WDCI signed an agreement (the “Agreement”) to combine the business and operations of the four Cooperatives into a single cooperative marketing association to be known as Dairy Farmers of America, Inc. The Agreement was approved by the Board of Directors of each of the Cooperatives. The Board of Directors of each of the participating Cooperatives also reviewed and approved the forms of Articles of Incorporation and Bylaws of DFA, the terms of separation of the Southern Region from AMPI, the agreement and plan of merger (the “Merger Agreement”), the governance and areas of DFA, the DFA Capital Plan, and the terms and conditions under which the four Cooperatives would be combined and DFA would conduct its operations, all of which were set forth in a Term Sheet, the material terms of which are described in this Statement of Terms. A vote in favor of the merger means approval of the transactions described in the Agreement, including approval of the DFA Articles of Incorporation, Bylaws, Capital Plan, Merger Agreement, and the initial members of the Board of Directors of DFA, the Area Councilpersons and the Delegates and Alternate Delegates, all of whom will serve during the three-year transition period.

The Merger Agreement

The Merger Agreement is the legal document governing the merger of Southern AMPI, MMI, and WDCI with and into DFA (the “Merger”). A copy of the Merger Agreement may be obtained from your Cooperative. If the Merger is approved, memberships in AMPI, Mid-Am, MMI, and WDCI will become memberships in DFA. Each Member’s equity account with their current Cooperative will be transferred into a capital account of the same dollar value with DFA. DFA will not issue certificates evidencing equity ownership.

Each of the participating Cooperatives will make representations in the Merger Agreement as to the accuracy of its financial statements and certain other information. If during the two years following the Merger, the representations prove to be inaccurate and DFA incurs costs exceeding 2% of its total equity in the first year, or 5% of its total equity in the second year, then the amount of such excess will be charged against the capital accounts of members of that particular participating Cooperative.

Following the Merger, the business and operations currently conducted by Southern AMPI, Mid-Am, MMI, and WDCI will be conducted by DFA, and the separate existence of Southern AMPI, MMI, and WDCI will cease.

Reasons for the Merger

The Merger will combine the participating Cooperatives’ strengths to create a preeminent dairy cooperative with a strong market position in each of the six Areas. The dairy industry is becoming increasingly competitive and the greater strength of the combined entity will enable it to better serve existing members and customers, as well as provide members with substantial benefits. DFA will have the following strategic objectives:

• To enhance the bargaining position of member dairy farmers in a deregulating market.
• To achieve cost savings for members and customers through economies of scale.
• To participate in the development, production and marketing of value-added dairy products.
• To consistently provide high-quality products and services to members and customers.
• To institute a sound, equitable capitalization program which permits continued growth, profitability, and a market rate of return on investment.
• To develop an international market for products of DFA.

Potential Disadvantages of the Merger

Members/Delegates of Southern AMPI, Mid-Am, MMI, and WDCI should consider the following matters in deciding whether to vote in favor of the Merger. These matters should be considered in conjunction with the other information included and incorporated by reference in this Statement of Terms.

• Although upon approval of the Merger all members will automatically become members of DFA, it is possible that some members will decide to leave DFA upon the expiration of their marketing agreements.
• DFA will be subject to the restrictions of the antitrust consent orders currently applicable to AMPI, Mid-Am, and WDCI.
The development of new products and new markets will impose additional costs and may not result in higher margin products or additional net revenue.

Value-added products require an investment of capital, with benefits to be realized over time.

DFA will require a major investment to reconfigure information systems.

The management challenges of integrating operations of four Cooperatives may be greater than anticipated.

The proposed governance structure for DFA may be difficult, particularly during the three-year transition period.

**Recommendations of the Boards of Directors**

The Board of Directors of each of the participating Cooperatives believes that the Merger is fair to its members and in their best interests. The Board of Directors of each of the participating Cooperatives recommends a vote "FOR" the proposal to approve the Merger and effect the combination.

**Regulatory Process**

The Cooperatives are prohibited by U.S. antitrust laws from completing the Merger until they have furnished certain information and materials to the Antitrust Division of the Department of Justice and the Federal Trade Commission and a required waiting period has ended. Each of the Cooperatives will file the required notification and report forms with the Antitrust Division and the Federal Trade Commission.

The participating Cooperatives will be required to make filings with or obtain approvals of certain other regulatory authorities in connection with the Merger.

The participating Cooperatives must obtain consents or waivers from third parties in connection with certain financing arrangements and contractual undertakings to which they are parties.

It cannot be predicted whether DFA will obtain all required regulatory approvals before completing the Merger, or whether any approvals will include conditions that will be detrimental to DFA. It is a condition to completion of the Merger, however, that all required regulatory approvals be obtained.

**Member/Delegate Approval**

The Merger proposal must be approved by the affirmative vote of the Members/Delegates of each of the participating Cooperatives.

Meetings of the Member/Delegates of Southern AMPI, Mid-Am, MMI and WDCI will be held before December 1, 1997 to vote on the Merger proposal. The notice of meeting and other materials will be sent to the voting members or delegates.

**Conditions to the Merger**

The Merger will be completed only upon satisfaction or (in some cases) waiver of several conditions, including the following:

- the Member/Delegates of Southern AMPI, Mid-Am, MMI, and WDCI properly vote to approve the Merger;
- no legal restraints or prohibitions exist which prevent the consummation of the Merger, limit the conduct of a material portion of the business of DFA, or are likely to have a material adverse effect upon it; and
- prior to the Merger, there is no material adverse change with respect to the business or operations of any participating Cooperatives.

**Federal Income Tax Consequences**

It is expected that the transfer of membership interests effected in the Merger will be tax-free for federal income tax purposes.

**Corporate Governance**

The corporate governance structure of DFA is designed to have each of the six geographic Areas represented on the Board of Directors with an equal balance between producing units and volume delivered as factors in determining director representation. The governance structure allows for a strong grass-roots organization, so that DFA may be responsive to its members needs.

**Directors and Area Councils of DFA**

During the first three years following the effective date of the Merger, the Board of Directors of DFA will consist of the current directors (those in office as of January 1, 1998) of
the participating Cooperatives. Following this transition period, the Board of Directors of DFA will consist of 36 individuals elected on a formula basis to represent not only the number of producing units in DFA, but also the volume of milk produced by the six Areas. To effect this formulated representation during the transition period, each director will have a fractional vote, so that the total number of votes is 36 weighted to achieve both the producing unit and volume limitations.

A complete list of the initial Board of Directors of DFA and the members of the six Area Councils is available from your Cooperative. A vote in favor of the Merger is a vote to approve the individuals named to be members of the initial Board of Directors and members of the six Area Councils.

The permanent board structure of 36 individuals representing each of the six Areas will be implemented effective January 1, 2001. Each Area will be entitled to a number of directors based on the following formula:

\[
\text{Directors from each Area} = \frac{\text{Pounds of member milk marketed annually in an Area}}{\text{Pounds of Member milk marketed annually by DFA}} \times 18 + \frac{\text{Farms in an Area}}{\text{Farms in DFA}} \times 18
\]

Directors from each Area will be nominated by Area Councils and elected at the annual delegate meeting by a vote of all delegates. Each director will have a term of office of two years, except for the first permanent board where one-half of the directors will have one-year terms to achieve staggering.

### Board Committees

The DFA Board of Directors will select an Executive Committee of 12 directors to monitor the day-to-day business and affairs of DFA. The initial Executive Committee will consist of the 12 current members of the Consolidation Steering Committee. In 1998, DFA expects to have four committees with the following chairpersons:

- Chairperson of the Board and Executive Committee: Herman Brubaker
- Chairperson, Operations/Marketing: Carl Baumann
- Chairperson, Finance: Charles Beckendorf
- Chairperson, Public Policy and Government Relations: Tom Camerlo

Board officers in 1999 and 2000 will be selected by the Executive Committee. Compensation of directors and officers will be recommended by the Consolidation Steering Committee.

### Local Governance Bodies

The membership of DFA will be divided into six Areas. Each Area will have an Area Council which will monitor the business and affairs of DFA in its Area. Area Councils will provide advice and counsel to the DFA Board of Directors and its management. Area Councils will have a maximum of 36 members and each Area Councilperson will have one vote. An individual must be an Area Councilperson to be eligible to serve on the DFA Board of Directors.

Within each Area, an Area Council will establish Districts. The number of Districts and the location, function and structure of each District will be decided by the Area Council, but each Area must have at least two Districts. Although not required, Area Councils may elect to further subdivide their Area into Regions (made up of a number of Districts) and Locals (subdivisions of Districts). The number, location, function and structure of Regions and Locals are to be decided by the Area Councils.

DFA will have a delegate body. Delegates will be selected by members and will have authority to vote on all matters requiring approval by the membership. Each Area will have a number of delegates equal to the number of producing farms in the Area divided by 50. Delegate selection will be supervised by the Area Councils following uniform rules and procedures to be adopted by the DFA Board of Directors.

### Election Procedures

DFA Board Directors from an Area will be nominated by the Area Council from among its own members. Additional nominations may be made by the delegates from the floor of the delegate meeting at which directors are to be elected. Nominees are then voted on by the delegate body. The process to elect representatives to Area, Region, District, and Local organizations will be proposed by the interim Area Council for approval by the DFA Board of Directors. At member meetings, all voting will be done on the basis of one member, one vote.

### Interim Area Council Structure

As noted above, during the three-year transition period, existing local board members and delegates will be assigned to the Area, Region, District, Local, and delegate structures,
all under rules and procedures to be adopted by the DFA Board of Directors.

**Pay Prices**

DFA's pay prices will be based upon supply and demand factors and are expected to be different in each Area. Revenues generated in an Area from the disposition of milk produced in that Area will stay in that area and be incorporated into pay prices. Each Area will contribute to the programs of DFA and to the capital required to implement those programs. Each Area's milk pay prices will be established by the area management in consultation with the management of DFA. Area Councils will review the pay prices and policies.

**National Value-Added Functions**

DFA will establish two value-added divisions: manufacturing and bottling. The profits of the two value-added divisions will be allocated among the six Areas not less than annually. The manufacturing division profits will be divided in proportion to milk volume processed in DFA's manufacturing plants (whether commodity or value-added). The bottling division profits of DFA will be divided in proportion to fluid milk sales. As a consequence, every pound of milk sold by DFA will participate in either the manufacturing or bottling profit pools.

**Corporate Expenses**

DFA's corporate expenses will consist primarily of general, sales and administrative expenses and interest expense. General sales and administrative expenses will be allocated among the six Areas and the two value-added divisions on the basis of usage of the corporate functions by each Area and the divisions. Interest expense will be allocated among the Areas and divisions on the basis of net assets employed within each Area and division.

**Capital Plan**

**Objectives**

DFA has established a target aggregate capital base of 40% of its assets. Management of DFA believes that this will allow DFA to achieve the following objectives:

- To maintain a BBB credit rating or better.
- To establish a method of members providing capital in proportion to volume.
- To provide for allocation for net earnings on a patronage basis.
- To create guidelines for redemption of equities of inactive equity holders over a targeted 10-year period.

**Base Capital**

Each member and patron will have a base capital account equal to the stated value of capital retains and written notices of allocation. Capital accounts are non-voting, are subordinated to the debt of DFA and are subject to a lien permitting offset of member debts to DFA. The targeted base capital level will be $1.75 per cwt.

Base capital levels will be the per cwt. dollar amount derived by dividing the base capital account balance by base deliveries, which will be the annual average of deliveries for the two prior calendar years. Base capital levels will be determined once each year; provided, however, that for the first quarter of 1998, base capital levels will be calculated using reasonable estimates of December 31, 1997 capital account balances. As a result of the Merger, member equities of the four participating Cooperatives will be converted into capital accounts on a dollar-for-dollar basis.

Capital retains will be withheld at the rate of 10¢ per cwt. until a member has a base capital level of $1.00 per cwt.

Net earnings of DFA will be allocated on a cooperative basis. The form of allocation will be 20% cash and 80% qualified written notices of allocation until the base capital level reaches $1.75 per cwt. Thereafter, net earnings will be allocated 100% in cash.

Capital accounts may be transferred between family members of the same farm unit and between partners of a partnership on a single farm unit, if the partnership has been in existence at least two years.

Retirements of capital accounts will be at the sole discretion of the Board of Directors of DFA, but will be made in the following order of priority:

- estates;
- active members whose base capital level exceeds $1.75 per cwt., such that the excess is redeemed over a three-year period;
- members aged 60 or above on January 1, 1998 under the redemption plans of the four participating Cooperatives, who will be grandfathered and allowed to redeem under their current retirement plan; and
- others as determined by the Board of Directors of DFA.
DFA will operate on a cooperative basis and will allocate its net patronage earnings accordingly. DFA will not distribute any year amounts in excess of net earnings determined on the basis of generally accepted accounting principles. Revenues and expenses of DFA will be allocated among the six Areas. DFA will have two national value-added divisions: manufacturing and bottling. The manufacturing division will consist of secondary, demand-driven operations and other related operations. The bottling division will consist of the interests of DFA in various bottling ventures. Manufacturing division profits (or losses) will be allocated among the six Areas in proportion to the quantity of member milk going into DFA's plants or related manufacturing operations. Bottling division profits will be allocated among the six Areas in proportion to the quantity of member milk sold as bulk fluid (i.e. not going to a DFA plant). National division profits (or losses) will be allocated among the Areas at least once per year; provided, however, that $3 million of profits per year will be withheld and assigned to permanent capital. Corporate expenses will be allocated to the Areas on the basis of relative uses of corporate services and upon other equitable procedures as determined by the DFA Board of Directors.

Management of DFA will develop a business plan for each Area (working in consultation with area councils) which will provide for a 10¢ per cwt. profit margin starting with calendar year 2001. During the three-year transition period, profit margins are expected to be 6¢ for 1998, 7¢ for 1999, and 9¢ for 2000.

DFA will retain as permanent capital all earnings from business with non-members and such portion of earnings with members as deemed prudent by the DFA Board of Directors. Permanent capital will not be credited to member capital accounts.

Members of DFA will not be responsible for the debts of the association. The Board of Directors of DFA will provide for the payment of all financial obligations of DFA by modifying the Capital Plan and any other financial plans as may be needed, so that distribution of proceeds arising from the marketing of member milk will at all times be sufficient to pay all of the ordinary and necessary costs and expenses (including long-term indebtedness and accrued interest) of DFA.